

Agricultural Finance during COVID-19 and recovery: instruments and elements for a strategy

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Agriculture and agribusiness constitute a significant percentage of employment and still a sizable proportion of GDP in many developing economies, particularly in lower income countries. Incoming reports indicate that COVID-19 could have a significant impact on agriculture and MSME (Micro, Small and Medium Enterprise) agribusinesses through disruptions to the logistics, distribution, and production of food. At the same time, COVID-19 can be expected to further reduce the supply of finance to agriculture by adding to the challenges it faces among other things due to a) the heterogeneity and dispersion of farmers and MSME agribusinesses, b) the seasonal nature of production, c) the bulky finance requirements, and d) its exposure to political interventions. The timing of any financial support has to consider agriculture production cycles and logistics. This is critical to ensure continuous food production and distribution to consumers. Financing, even more than before, needs to look at the whole value chain, from farm to fork.

A strategy to address the impact of COVID-19 on agricultural finance should start with assessing the impact of COVID-19 on agriculture and take a granular approach (e.g. looking at the impact on different crops, value chains, regions, types of farmers, types of MSME agribusinesses, etc.). This will indicate the areas that require financial support and help determine the suitable instruments to deploy for specific circumstances and needs. Given limited resources during the crisis, the strategy should aim to target and prioritize the most affected areas keeping in mind economic efficiency and social objectives.

A. Assessing the impact

Given the urgency and limited resources, governments must very quickly assess the needs of the agricultural sector (primary production and agricultural businesses) stemming from the impacts of the COVID-19 and offer tailor-made incentives, packages, and instruments that satisfy those necessities accordingly. While enterprise survey tools could potentially enable the assessment of the impact of the COVID-19 on agriculture, such tools are usually not nimble enough to provide an actual picture of rapidly evolving developments, thus making it necessary to design and implement survey instruments that can be rolled out quickly and at low cost. This is critical to gain an adequate understanding of how limited government resources should best be allocated. For agriculture, the challenge is to assess the impact on the whole value chain, from farm to fork, including impacts on supply of inputs, production, storage, processing, distribution, etc. The dynamics of demand as well as supply are changing sharply due to the pandemic since important food consumption outlets such as restaurants, hotels, hospitality, etc. have substantially reduced demand, while most food consumption has moved to homes. On the supply side, due to the seasonality of supply, it is critical to ensure the timing of such assessments in order not to miss important crop cycle events.

The impact of COVID-19 can vary widely depending on crops and value chains. More specifically the assessment of impact could focus on the following issues:

- 1. Conduct diagnostics of specific agriculture value chains to understand the specific issues they face which will vary depending on the value chain.** This can include labor shortages,

loss of markets to sell products, disruptions in food logistics, and difficulties in accessing credit, etc.;

2. **Review existing programs and instruments that support agriculture (including farmers and agribusiness MSMEs) and agricultural finance** to identify the potential for scaling up and modalities for restructuring to meet the needs of the agriculture sector in crisis, and, where there are gaps, to recommend new programs and instruments. Identifying existing institutions and modalities that already are effective and reach out to farmers and agribusiness MSMEs will speed up the process for assessing and distributing programs;
3. **Bring in lessons learnt** from other countries to respond to the immediate needs of the agricultural sector;
4. **Build capacity** within governments to evaluate the impact of the present crisis on agriculture and to monitor the evolution as the situation may be rapidly changing. This would enable policymakers to adjust interventions accordingly. This capacity-building will also be a useful tool for the government to manage risks from crises in the future. However, building capacity could take time if not much is already in place. Governments could explore resources in place available by local and international institutions, associations or firms to monitor the impact and develop plans, These actors can be brought in to participate in government-led working groups and these groups or task forces could become permanent instruments that can be “beefed up” when needed now and in the future.

It is important to understand that responses to the crisis may differ by sector in a given country but also can differ between sub-sectors or value chains even if we take the case of agriculture. For example, in China, when entrepreneurs were asked in a post-coronavirus survey to list the two supportive policies they think are most needed, it became apparent that the requirements differed across sectors and directly relate to the specific problems each faces, be it shortage in labor, lack of consumer demand, disruptions in the supply chain, shortage of raw materials, etc. In agriculture, larger farmers for export oriented bulk agricultural commodities (e.g. grains and oilseeds) may face different conditions compared to smaller farmers of perishable commodities (e.g. fruits, vegetables, meats, etc.) for local consumption. The challenge in assessing impacts in agriculture, compared to other sectors, is the large degree of informality of smaller farmers and enterprises and their large dispersion in rural areas which makes collection of timely information difficult.

B. Supporting mechanism for agriculture and agricultural finance

A mix of instruments and approaches. Governments during crises need a “toolbox” of instruments that can be deployed in a timely fashion to address the needs of farmers and MSME agribusinesses. Such a toolbox should not only address the present COVID-19 crisis but also have the structures and systems in place for possible future crises. Given the special importance of agriculture for food safety, employment of the poor, and the environment, such toolbox should include measures to assist the economic actors involved in agriculture as well as the financial service providers that cater to them and that can provide much-needed support to help them overcome the consequences of COVID-19.

Depending on the diagnostic of the factors affecting the sector and the supply of finance to agriculture, the choice of instruments to be used will have to consider the existing support mechanisms, the level of development of the financial sector, the degree of financial inclusion of rural and agricultural households as well as the fiscal space/capacity of the government and the Central Bank to provide liquidity and funding. The measures to be taken in support of agricultural finance would complement any other measures taken to keep the agricultural value chains in

operation and minimize disruptions due to COVID-19. The instruments can be broadly divided into emergency responses and recovery support:

1. Emergency responses that aim at compensating and mitigating the impact of COVID-19 on farmers and MSME agribusinesses. These measures can be also applied in support of MSMEs in other sectors of the economy:

Well-targeted income support and matching grants. Since many firms that would otherwise be viable run into trouble and may become insolvent mainly due to the COVID-19, they would require measures that provide income support to survive a what could prove to be temporary situation or setback. Such support would enable them to resume their activities when the crisis subsides. Depending on where are exactly the problems, matching grants could be used for example to cover the fixed overhead costs of agribusinesses such as the payroll obligations to maintain the level of employment (prevent them from laying off workers) in the face of lower business volumes. According to a recent IMF paper titled "[Policy Steps to Address the Corona Crisis](#)", wage support for businesses affected by shutdowns can help prevent cascading bankruptcies and massive layoffs that will have lasting effects for future recovery and negative impact on aggregate demand¹. So far, most of the grant programs, aim to support retention of employment by firms (compensate the payroll of firms) and pay some other fixed costs (e.g. rent, utilities) for a certain period of time (e.g. for two to three months).

Given the scarce fiscal resources and the significant demands from every sector for support, governments should develop transparent criteria for such grants to maximize their economic impact and support truly viable companies confronting the COVID-19 crisis. Grants should have a clear purpose as to why they are given, what they aim to achieve, and be time-bound. Additionally, in order to maximize the economic impact of the grants, governments could consider prioritizing agribusinesses that are innovative (new production technologies), aim to improve business practices, and adopt environmentally friendly approaches (climate smart agriculture), etc. Also, to keep in mind that the recipient firms may benefit from access to technical assistance which the grants could cover. The matching requirement could be lower than usual in view of the urgency.

For smaller farmers, cash grants can support their income, and enable them to continue investing in agriculture (e.g. inputs, etc.), but equally importantly, enable them to maintain critical household expenses such as health care costs, school fees, and nutritious food, etc. in the face of the crisis that can lower their income (e.g. unable to sell because challenges in accessing markets) and increase their expenditures (e.g. health care). Responses to small holder farmers should be part of a strategy for social safety nets in the times of crisis.

Support to maintain or increase financing and prevent the rise of NPLs.

Loan repayment moratoria and restructuring. Loan repayment moratoriums and relaxing the classification of restructured loans by Central Banks can be very beneficial for agricultural businesses and farmers that face temporary difficulties in servicing their loans due to the current crisis. Viable businesses and farmers would need support to overcome what hopefully is a temporary set-back in their ability to service their loans, especially when for years they have shown good repayment behavior. In the case of seasonal agricultural production, restructuring may require longer periods of time than in the case of loans for other economic activities to allow farms to go through a new production cycle. On the other hand, restructuring should not impose big costs on

¹ Based on a survey of SMEs in February, reports on China showed that a third of SMEs only had enough cash to cover fixed expenses for a month, with another third running out within two months, putting millions of Chinese SMEs at risk. Similar situations may exist in many ECA countries.

banks in terms of higher provisions when loans are reclassified due to restructuring. This means that Central Banks may need to consider relaxing requirements for the classification of restructured loans and for the establishment of additional provisions by banks. Many governments, like the government of Malaysia, have imposed a moratorium on loan repayment for 6 months, which means no re-payment of principal and interest and without compounding the interest during the time of the moratorium.

Guarantees and lines of credit. During emergency times, lines of credit and credit guarantees can play an important role to sustain activities in agriculture. During the pandemic crisis, there is still need for credit, amid perhaps lower compared to the year before, for inputs, food processing, storage and food distribution activities. Many governments are providing subsidized credit and credit guarantees to commercial banks (and in some countries also to financial cooperatives and microfinance entities) to address the pressing needs of farmers and MSME agribusinesses during the pandemic. In contrast to lines of credit, which can be disbursed more easily, the use of credit guarantees requires that institutions and programs are already in place at the time of the emergency, as the process of setting up a new credit guarantee agency or scheme will usually require several months, if not years. Guarantees and lines of credit are discussed more extensively in the next section on recovery support.

Fiscal stimuli. Governments have several instruments as part of their fiscal policy arsenal, including tax rebates and tax cuts, social security reductions, and exemptions, etc. Such fiscal measures could take regional or even community-level approaches to support farmers and agribusinesses in specific areas of the country, agricultural value chains harder hit, or the chains that play a critical role in providing food to the population.

Equity investments by the state. In previous financial or economic crises, Governments took an equity stake to prevent the collapse of key large companies, as a temporary measure. A recent example due to the COVID-19 crisis some countries such as France, are also considering measures that would allow the state to temporarily take an equity position in companies to prevent them from going under. In the case of agriculture, this type of measures may be relevant especially for large systemic companies such as aggregators and processors that play a strategic role in the operation of the agricultural value chains.

2. Recovery support relates to support farmers and MSME agribusinesses to conduct their business both during the COVID-19 period and during the recovery. Again, like the emergency responses, the instruments presented here can be applied for the same purposes for MSMEs in all the sectors of the economy. The critical feature of agriculture is timing. Given that financing for agriculture and MSME agribusinesses is linked to crop calendar, it is critical to have the available credit and guarantees timed to meet the seasonal production cycles in agriculture.

Credit guarantees (Partial Credit Guarantees) can become a powerful instrument to enable banks and other qualifying financial institutions to continue lending to agriculture during and after the crisis and for businesses to re-start their activities when the crisis subsides, and new credit is needed. Partial credit guarantees are particularly effective during times of increased uncertainty and risk aversion by financial institutions. During a crisis, if demand for credit due to low level of economic activity dries up, credit guarantees will be of limited use. Such credit guarantees influence more the supply side, enabling the banks and other entities to lend in difficult conditions. At the same time, financial institutions exercising outstanding (existing) credit guarantees may not be prudent since for no fault of their own, borrowers may be experiencing difficulties in loan repayment due to the COVID-19 crisis. In this scenario, claiming the guarantees by financial institutions means that the borrowers are in default. This automatically leads to closing the account and starting

foreclosure procedures. This also means that the borrower may get a negative record at the credit bureau and may have difficulties accessing new funding in the future. For these reasons, claiming on the guarantees, particularly for otherwise creditworthy and viable borrowers should be avoided. Banks and other financial institutions usually do not claim on guarantees if they believe the borrower is viable and they will try to keep the borrower “alive” through restructuring. Temporary moratoriums can help taking out any discretion about putting claims in the system.

Credit guarantees would be valuable in the recovery period when businesses would need fresh funding to resume or scale up operations. With firms and farmers having their previous debt (through restructuring or moratorium) in place, their collateral being committed already, partial credit guarantees can provide the much-needed collateral for banks to resume lending even if parts of their previous debt are still outstanding. Several countries, as a response to the COVID-19, have increased the coverage (e.g. up to 90% and some countries up to 100%) of the guarantees, increased the maximum amount of loan benefiting from the guarantees, extended the maturity of loans eligible for guarantees (e.g. up to 7 years), in some cases waived the guarantee fees, and simplified and expedite procedures for application and approval. While such measures can significantly enhance the use of guarantees, they may also create moral hazard on the side of the financial institutions and unrealistic expectations of borrowers. It is therefore strongly advised that increases in coverage (and other terms made more flexible) are carefully designed to maintain the accountability of the lending institutions in recovering the loans and that their temporary nature is clearly communicated to lenders and borrowers.

Credit guarantees require strong institutional setting and to function well they have a number of requirements (see 16 principles for partial credit guarantee funds)²². Key amongst them, are proper governance, ensuring financial sustainability, operational modalities, risk management, and M&E. If countries do not have existing guarantee schemes, it will take time to set them up and even longer to implement and scale them up, while it is more complicated to find adequate set-up and right design features during a crisis, particularly trying to balance reach with financial sustainability. Nevertheless, even countries without existing guarantee institutions, they may take the present opportunity and start setting up ones which although may not help with the emergency response and immediate post recovery response, they can play an important role when they will become operational in due time. And, of course, help for the next crisis if and when it arises.

Lines of credit. If liquidity proves to be a problem for financial institutions to lend to agriculture, specific lines of credit could be considered for on-lending to particular sub-segments of agriculture and those MSME agribusinesses whose credit access was the most affected due to the COVID-19 crisis. For continuing funding during COVID-19, governments might consider lowering the cost of finance to small farmers and MSME agribusinesses for loans amounts up to a certain level and for specific purposes. Such a low-cost credit program should be targeted in both its use and its beneficiaries, time-bound (sunset period), and will need a strong M&E framework to ensure that it is used as intended and has the desirable results. A number of countries report government programs that provide low cost financing at subsidized rates, and in some cases at zero interest rate, for immediate financing needs (working capital) of farmers and agribusiness MSMEs. Lines of credit for agricultural annual food crops may be important given the increase in self-sufficiency needs for food as a result of disruptions in imports during the pandemic. In addition, the trends for increased food processing, storage, improved food safety standards, efficient logistics particularly

²² . In 2015, the World Bank together with international associations of PCGSs and lenders published the [Principles for PCGSs for SMEs](#), a set of good practice principles to guide the design, execution and evaluation of PCGSs around the world.

for retail sales, will be even more pronounced in the post COVID-19 period which means increased need for new investments in these areas.

Key considerations to maximize the impact:

Looking beyond commercial banks. In most countries, commercial banks are the main target and channel of support to firms, including MSMEs. However, when it comes to agriculture and agribusinesses, commercial banks tend to cater more to medium and larger farmers and small and medium agribusinesses, and perhaps to small holder farmers and smallholder farmer organizations in well-structured value chains and commercial crops. This can leave a large number of small holder farmers and micro small informal businesses engaged in food production and distribution outside the support system. Channels to reach to these farmers and micro and small agribusinesses in the food sector would need to include microfinance institutions, small local banks, and cooperative financial institutions, etc. which are usually smaller than commercial banks. These institutions may require dedicated lines of support as they tend to cater more to the smaller types of clients in agriculture and rural areas including the ones at the bottom of the pyramid. As financial cooperatives and microfinance institutions are oftentimes the main providers of financial services to smallholder farmers and to agricultural MSMEs, it is important that the loan portfolios of such entities can also be covered by partial credit guarantees during recovery. Considering that the loan portfolios of these institutions are composed by large numbers of loans, guarantees should be issued in these cases using a “portfolio approach” and not by assessing and covering each borrower individually. In addition, measures may be needed to facilitate access by these entities to funding as they in most cases do not have access to the funding and liquidity facilities that are available to banks. In some countries, complementary measures may therefore be considered, including dedicated lines of credit for MFIs and financial cooperatives, or partial credit guarantees that cover the loans granted by banks and commercial funds to such entities.

Going digital. In the times of pandemics like COVID-19, reliance on efficient ways to assess loans and distribute money without physical contact becomes critical. Several commercial banks are moving to an automated system for loan processing without visiting clients. The loans are disbursed into e-wallets or bank accounts that can be accessed through e-banking. This kind of arrangement is available mainly for existing clients, for now, so having a pre-existing relation with a bank or a financial institution becomes crucial. At the same time, digital accounts enable faster and efficient distribution of G2P payments during a crisis such as COVID-19. The need for digital payment channels becomes even more important as these channels are critical to support the rapidly evolving e-commerce platforms that sustain economic activity and commerce during pandemics. Smaller financial institutions outside the digital payment network must catch up in this regard, investing in technologies that allow them to modernize the way, in which they interact with their members and clients. Such technologies can help farmers and MSME agribusiness use new digital payment systems and e-commerce platforms to sell their produce and purchase goods they need (e.g. inputs, etc.). As the abovementioned smaller financial institutions cannot be expected to develop their own digital delivery platforms, this route will likely increase the relevance of partnerships with other similar financial institutions, aggregators, and FinTech firms to help them enter the digital market.

Although so far countries have been focusing more on broad strategies to assist small and medium firms in all sectors of their economy, in response to COVID-19, agriculture would deserve special attention given its economic, environmental, social, and regional impacts in countries. Support to financing agriculture responding to COVID-19 at least for now is a mixture of income support to farmers and measures to support MSMEs in general that of course include agribusiness MSMEs (but nothing specific for agribusinesses).

Observations from the client countries

The Asia-Pacific Rural and Agricultural Credit Association (APRACA) conducted a survey to understand the preparedness and responses of its members across the region. Twelve institutions (mostly public banks specialized in rural and agriculture finance) from 9 countries responded. The complete survey results are available from [this link](#). All the respondents are already seeing a negative impact on the agriculture sector mainly due to supply chain disruptions, and labor shortages. Some expect that the crisis may lead to food shortages (Nepal). At the same time, these financial institutions anticipate that their loanable funds would decrease caused by withdrawals, fewer deposits, and loan defaults (India, Vietnam). Nonetheless, they started supporting their rural and agriculture clients by rescheduling loans, reducing interest rates, waiving charges for internet banking transactions, and providing new loans. Some institutions promote and strengthen their digital financial services (China, India). The governments support financial intermediation by introducing credit lines, expanding partial credit guarantees and reducing interest rates, etc.

Similarly, ALIDE, the Latin American Association of Development Banks, many of which have a mandate to serve agriculture, [reports a series of actions](#) that have been undertaken in that region [link]. These actions include special lines of credit to ensure the business continuity of farms and processors, as well as of the transport and logistics companies that bring store and transport agricultural produce to market. These lines of credit are being funded with own resources and with special lines for agriculture, which is one of the sectors most affected by the pandemic. In addition, these development banks have introduced greater flexibility in their funding, allowing to extend loan maturities, reducing interest rates, and facilitating access to insurance. In addition, these banks have also introduced guarantees and lines of credit for microfinance institutions this allowing this type of institutions to access funding and to continue their lending to smallholder farmers and agricultural MSMEs. In some countries, similar measures were extended to the input suppliers and processors of agricultural produce that engage in financing their suppliers and/or client farmers. Governments on the other side have supported in Latin America these activities by granting guarantees to development banks so that these can access financing themselves at favorable conditions in the market. As an additional measure for second-tier providers of finance, some governments have also relaxed the regulatory that usually constrain the access of these entities to third-party funding. In the case of the agricultural insurance, the governments have strengthened their equity and increased in some countries the premium subsidies for agricultural insurance aiming to increase the coverage of insurance for agricultural loans.